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Before the  
Federal Communications Commission  
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION

In the Matter of )

)  
Amendment to The Bell Atlantic )  
Telephone Companies )  
Tariff FCC No. 10 )

)  
Video Dialtone Service )

Transmittal Nos. 741, 786  
Amended

CC Docket No. 95-145

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REPLY OF BELL ATLANTIC  
TO COMMENTS AND OPPOSITIONS  
CONCERNING DIRECT CASE

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## TABLE OF CONTENTS

	<u>PAGE</u>
I. Introduction and Summary . . . . .	1
II. Bell Atlantic's Rates Recover Its Costs of Providing Video Dialtone Service . . . . .	4
A. Telephone Rate Payers Will Not Cross-Subsidize Video Dialtone Services . . . . .	4
B. Bell Atlantic's Tariff Prices Are Appropriately Based on the Costs of Providing Video Dialtone Service over the Dover Network, Not A Hypothetical Network . . . . .	8
C. Bell Atlantic's Method of Allocating Common Costs is Lawful and Reasonable . . . . .	11
D. Bell Atlantic Has Properly Allocated Other Costs to This Video Dialtone Service . . . . .	15
E. Bell Atlantic Has Properly Redacted Proprietary Vendor Pricing Information . . . . .	20
III. Provision of Digital Converters and Network Interface Software are Non-Regulated Services . . . . .	22
IV. The Other Objections to This Tariff are Meritless . . . .	28
CONCLUSION . . . . .	35

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I. INTRODUCTION AND SUMMARY

The Commission is faced with a clear choice in this proceeding: to continue to evaluate tariffs under the "not patently unlawful" standard that it has applied for 60 years in accordance with its statutory mandate,<sup>2</sup> or to impose unlawfully a new standard for video dialtone service that would, in effect, allow the telephone company's competitors to dictate the type of network that the telephone company may deploy and the terms of the services it may offer.

The Commission's decision on this issue will have far-reaching implications. If the Commission applies new, more stringent and erroneous standards to its evaluation of the lawfulness of this video dialtone tariff that result in unreasonable, unfair and overly burdensome allocations of the costs

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<sup>1</sup> The Bell Atlantic Telephone Companies ("Bell Atlantic") are Bell Atlantic-Delaware, Inc., Bell Atlantic-Maryland, Inc., Bell Atlantic-New Jersey, Inc., Bell Atlantic-Pennsylvania, Inc., Bell Atlantic-Virginia, Inc., Bell Atlantic-Washington, D.C., Inc., and Bell Atlantic-West Virginia, Inc.

<sup>2</sup> 47 U.S.C. § 201(b).

of network upgrades to a single new video service, the Commission will ensure that its dream of encouraging effective competition to cable through open common carrier networks will never be realized. Despite hundreds of pages of misleading and erroneous claims against Bell Atlantic's Dover Township video dialtone tariff, the cable industry agrees with Bell Atlantic on one fundamental fact: "In addition to deciding how the costs of Bell Atlantic's Dover facility will be allocated, this proceeding also will establish precedent that will guide the investment decisions of other local exchange carriers."<sup>3</sup>

As the cable industry correctly gloats, its campaign of fear and intimidation, as well as regulatory gamesmanship, has led many carriers to conclude that the game is not worth the candle: rather than pursue the open network vision, they are wearily agreeing simply to be cable clones. Although the Commission and Congress are striving to clarify the regulatory framework for these open common carrier platforms in a way that enables competition to flourish, it will all be for naught if the cable industry succeeds in forcing competitors to bear unreasonable cost allocations and

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<sup>3</sup> Opposition of Adelphia Communications Corp. to Bell Atlantic's Direct Case, at 2 (Nov. 30, 1995) ("Adelphia Opp."). See also Opposition to the Bell Atlantic Direct Case of Cox Enterprises, Inc., at 3 (Nov. 30, 1995) ("Cox Opp.") ("the precedential value of the Commission's determinations in Dover will have an enormous effect on other LECs proposing video dialtone networks."). Of course, cable is focused on the "extremely remote" possibility of cross-subsidization of video services by telephone ratepayers, see Supplemental Affidavit of William E. Taylor, Ph.D., ¶ 22 (Dec. 20, 1995), attached as Exhibit B ("Supplemental Taylor Aff."), rather than the very real risk of unfairly burdening video services with unreasonable costs.

therefore to be priced out of the market. It will not be in the public interest, or to the benefit of consumers, if the Commission were to order modifications to Bell Atlantic's video dialtone transport rates that disadvantage its programmer-customers and protect the incumbent cable operators from full and fair competition. Moreover, given the Commission's proposal to waive rate regulation for cable operators in Dover Township,<sup>4</sup> requiring video dialtone programmer-customers to pay higher rates could simply create a higher umbrella under which cable operators could raise their prices, to the detriment of consumers.<sup>5</sup>

Many objections raised by commenters have already been exhaustively addressed by Bell Atlantic in earlier filings in this proceeding.<sup>6</sup> Bell Atlantic therefore will not reiterate all of the arguments that it has already made, but will focus primarily on those issues raised by parties for the first time or variations on previous arguments. In this Reply, Bell Atlantic again

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<sup>4</sup> See Order Requesting Comments, **Waiver of the Commission's Rules Regulating Rates for Cable Service**, CUID Nos. NJ0213, NJ0160, FCC 95-455 (rel. Nov. 6, 1995).

<sup>5</sup> See **Waiver of the Commission's Rules Regulating Rates for Cable Service**, CUID Nos. NJ0213, NJ0160, FCC 95-455, Reply of Bell Atlantic, at 4 (Dec. 13, 1995).

<sup>6</sup> See Reply of Bell Atlantic (filed Mar. 6, 1995) ("Tariff Reply"); Transmittal No. 741-Amended (filed May 5, 1995); Letter from Marie Breslin, Bell Atlantic, to Geraldine Matise, Chief, Tariff Division, Federal Communications Commission, dated May 5, 1995; Letter from Joseph Mulieri, Bell Atlantic, to David Nall, Deputy Chief, Tariff Division, Federal Communications Commission, dated June 7, 1995; Reply of Bell Atlantic (filed May 19, 1995); Bell Atlantic Direct Case (filed Oct. 26, 1995) ("Direct Case"); Bell Atlantic Opposition to Motion for Extension of Time (filed Nov. 22, 1995).

demonstrates that its rates, in compliance with the Commission's rules, will cover its costs of providing this video dialtone service, and that the terms and conditions of its tariff are commercially reasonable and nondiscriminatory. In addition, Bell Atlantic explains why provision of customer premises equipment and other services related to video dialtone not only should, but must, continue to be provided as non-regulated services.

Some of the comments filed also reflect confusion about whether information is or is not in the record, or a misunderstanding about what the data Bell Atlantic has provided means. A number of these issues are addressed in Exhibit A to this Reply.

**II. Bell Atlantic's Rates Recover Its Costs of Providing Video Dialtone Service**

Four primary criticisms have been raised concerning Bell Atlantic's allocation of costs to video dialtone service on the upgraded Dover Township network. These criticisms are unfounded. They are inconsistent with the Commission's rules, contrary to economic theory, and are transparently intended to force Bell Atlantic's prices for this service to uneconomic levels in order to prevent effective competition in the video market.

**A. Telephone Ratepayers Will Not Cross-Subsidize Video Dialtone Service.**

First, critics assert that telephone ratepayers will be cross-subsidizing this video dialtone service if the cost of the entire network upgrade in excess of the cost of a standalone

narrowband network is not allocated to this video dialtone service.<sup>7</sup> The cable industry's confusion that such cross-subsidization could occur is based on a false dichotomy: that all costs must be allocated either to the first video service on the network -- video dialtone -- or to existing telephone services.<sup>8</sup> Instead, the costs of the network upgrade will be allocated to and recovered from revenues from the broad variety of narrowband and wideband voice, video and data services that this network will be able to support,<sup>9</sup> such as extended local area networks and high-speed Internet access and data services (including access to

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<sup>7</sup> See Adelphia Opp., at 10; Opposition to Direct Case of New Jersey Cable Television Ass'n, at 3-4 (Nov. 30, 1995) ("NJCTA Opp."); Opposition to Direct Case of National Cable Television Ass'n, at 13-17 (Nov. 30, 1995) ("NCTA Opp.").

<sup>8</sup> See Declaration of Leland L. Johnson, Ph.D., at 5-7, 9-11, ("Johnson Decl."), attached to the oppositions filed by New Jersey Cable Telephone Ass'n, Adelphia Communications Corp., and National Cable Television Ass'n.

<sup>9</sup> As Bell Atlantic has previously noted, it is irrelevant whether Bell Atlantic could provide these services by otherwise upgrading existing facilities. Moreover, the speed and other performance characteristics of these same services over narrowband networks would be significantly inferior to those services when offered over broadband networks. The higher cost of individual versus network construction would also make the service uneconomical for many customers. Indeed, it is the construction of an upgraded network that provides the economies of scope to support many services, which will itself spur market acceptance of these new services. See Letter from Edward Shakin, Bell Atlantic, to Mr. William Caton, Acting Secretary, Federal Communications Commission, dated Feb. 16, 1995, at 11 n.46.

multimedia libraries and other interactive databases).<sup>10</sup> How shared costs will be assigned to -- and what prices will be charged for -- Bell Atlantic's various narrowband or broadband voice, video or data services other than video dialtone will be addressed in other tariff proceedings.

Consistent with well-recognized basic economic principles, Bell Atlantic's video dialtone prices, which recover all of the direct costs caused by the provision of video dialtone service in Dover Township (as defined by the Commission's rules),<sup>11</sup> plus a reasonable allocation of overhead costs, "involve neither cross-subsidy nor predation because they necessarily exceed the forward-looking incremental costs of the service."<sup>12</sup>

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<sup>10</sup> Advanced facilities, such as those being deployed in Dover, are especially suited to the provision of services such as high speed Internet access, diskless network access stations, and the transport of large digital objects -- such as program files or still images -- with negligible delay, for example, more sophisticated distance learning and tele-medicine applications. See Supplemental Affidavit of Dr. Charles L. Jackson, ¶¶ 5-7 (Dec. 20, 1995), attached as Exhibit C ("Supplemental Jackson Aff.").

<sup>11</sup> **Telephone Company-Cable Television Cross-Ownership Rules, §§ 63.54-63.58**, 10 FCC Rcd 244, ¶¶ 217-19 (1994) ("VDT Recon Order").

<sup>12</sup> See Supplemental Taylor Aff., ¶¶ 3-5.



Moreover, both the Commission<sup>13</sup> and New Jersey state regulators<sup>14</sup> have explicitly rejected the cable industry's repeated allegation that additional video dialtone-specific cost allocation rules are required to prevent cross-subsidization. Cable claims that, despite the existence of price cap regulation at both the federal and state levels, the link between costs and prices has not been broken because of two remaining indirect links: (1) the sharing mechanism under the New Jersey price cap plan, and (2) the fact that regulators will have a chance to review and adjust price cap regulations after a set number of years. But as Dr. Taylor explains, those attenuated links hardly give Bell Atlantic any incentive to undertake a possibly unprofitable investment in the video dialtone business in the hope that in some way, now or later, it could recoup some of those costs from regulated ratepayers.<sup>15</sup>

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<sup>13</sup> See VDT Recon Order, ¶ 169.

<sup>14</sup> The New Jersey Board of Regulatory Commissioners (since renamed the Board of Public Utilities) considered and rejected concerns that the accelerated investment for these network upgrades would be cross-subsidized by telephone ratepayers. Decision and Order, **Application of New Jersey Bell Tel. Co. for Approval of its Plan for an Alternative Form of Regulation**, Docket No. TO92030358, at 106 (rel. May 6, 1993) ("After careful review . . . the Board FINDS that [the Board's cost allocation system] is an appropriate non-structural safeguard to ensure that the costs of [Bell Atlantic-New Jersey] are properly allocated and to ensure that cross-subsidization does not occur." (emphasis in original)). In addition, rates for basic telephone service have been frozen through 1999 as an added protection for ratepayers.

<sup>15</sup> See Supplemental Taylor Aff., ¶¶ 17-22.

Finally, despite commenters' fears,<sup>16</sup> any losses sustained by this video dialtone service if prices do not cover costs will indeed be absorbed by Bell Atlantic's shareholders, not by telephone ratepayers. Because Bell Atlantic is under no sharing price cap plan, and the Commission has proposed no sharing going forward,<sup>17</sup> there is no link between the cost of the video dialtone system and Bell Atlantic's ability to raise interstate prices. The risk of any new interstate service, including video dialtone, is on the shareholders.

**B. Bell Atlantic's Tariff Prices Are Appropriately Based on the Costs of Providing Video Dialtone Service over the Dover Network, Not A Hypothetical Network**

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Second, the cable companies assert that in order to prevent cross-subsidization of video dialtone service by telephone ratepayers, Bell Atlantic should be required to allocate to video dialtone service all costs in excess of those required to maintain or upgrade a standalone network to support only narrowband services.<sup>18</sup> Their arguments are irrelevant to this proceeding, and are simply wrong. The only issue that the Commission may lawfully decide in this proceeding is whether Bell Atlantic has

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<sup>16</sup> See Cox Opp., at 5-6.

<sup>17</sup> See **Price Cap Performance Review for Local Exchange Carriers; Treatment of Video Dialtone Services Under Price Cap Regulation**, Second Report and Order and Third Further Notice of Proposed Rulemaking, CC Docket No. 94-1, ¶ 36 (rel. Sept. 21, 1995).

<sup>18</sup> See, Johnson Decl. at 2, 5-7, 15-19; NJCTA Opp., at 6-7; Adelphia Opp., at 10-13; NCTA Opp., at 13-17.

properly allocated to a particular new service -- video dialtone -- the costs required to be allocated to that service under the Commission's rules, based on the actual equipment used to provide this service over the Dover upgraded network -- not some other hypothetical network.

As a threshold matter, cable's argument calls on the Commission to substitute for Bell Atlantic's business judgment the views of its competitors concerning the optimal or most socially desirable network configuration for delivering a broad array of existing and future services to Bell Atlantic's customers. As Bell Atlantic has previously explained at length in other proceedings to which the Commission is a party, in Bell Atlantic's business judgment, it is neither economically efficient nor prudent to build and maintain two separate standalone networks to support narrowband and broadband services, respectively.<sup>19</sup> As a result, Bell Atlantic has chosen to upgrade the Dover network to provide a full range of video, voice and data services on an integrated basis.

The cable industry is inappropriately seeking, at the tariff stage, to revisit arguments that were reviewed and rejected

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<sup>19</sup> See Plaintiffs' Reply Memorandum in Support of Their Motion for Summary Judgment, Appendix, Supplemental Declaration of Mark Wegleitner (filed Oct. 30, 1995), United States Tel. Assn. v. Federal Communications Commission, Civ. Action No. 95-533-A (E.D.Va.), attached as Exhibit D. See also *id.*, Supplemental Affidavit of Thomas W. Hazlett, ¶ 3 ("The economies of scope that can be realized from the use of common facilities to provide both telephony and cable offer potential savings that are likely to have a very large impact on when -- and even whether -- robust competition emerges in multichannel video markets"), attached as Exhibit E.

by the Commission during the Section 214 authorization proceedings,<sup>20</sup> and by New Jersey state regulators during hearings on approval of Bell Atlantic's Opportunity New Jersey plan. The New Jersey Board of Regulatory Commissioners, after reviewing in detail Bell Atlantic's network upgrade plans, required construction of these advanced integrated facilities with both narrowband and broadband capabilities, in conjunction with Bell Atlantic's Plan for Alternative Regulation, because such facilities will "enhance economic development while maintaining affordable rates, . . . promote diversity in telecommunications products and services and [] encourage the maximum efficiencies of the public switched network."<sup>21</sup>

Since both the Commission and the New Jersey Board have already authorized construction of this upgraded integrated network, the only question to be addressed in this tariff proceeding is whether the costs of the equipment actually used in this network have been properly allocated to video dialtone service. Other possible standalone systems are of no relevance to that inquiry, as is clearly demonstrated by the fact that the cost allocation approach advocated by cable would require the Commission

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<sup>20</sup> **New Jersey Bell Tel. Co.**, 9 FCC Rcd 3677, ¶ 1, (1994) ("Dover 214 Order") (holding that New Jersey Bell's plan to upgrade its Dover network to provide video and voice services on an integrated basis "will promote the 'public convenience and necessity' in Dover Township").

<sup>21</sup> See Decision and Order, *Application of New Jersey Bell Tel. Co. for Approval of Its Plan for An Alternative Form of Regulation*, Docket No. TO92030358, at 96-97 (rel. May 6, 1993).

to order Bell Atlantic to base its prices for this service on some third party's estimate of what Bell Atlantic's costs might be for a network that it is not actually building.<sup>22</sup>

Moreover, even if cable's argument had some relevance to the issues in this proceeding, the Commission has previously considered and rejected the substance of that argument with regard to the Dover system. The Commission observed:

[B]ecause the telephone network is constantly being upgraded, the question is not simply whether or not all costs above the existing costs of telephony should be assigned to video dialtone service. Rather, the issue is how much of the costs are incremental to the cost of providing an expanding array of services over the telephony network. In other words, it is incorrect to view all changes to the present telephone system as incremental to video dialtone service because a portion of those changes would have been made to the system as part of the normal upgrade, with or without the decision to provide video dialtone.<sup>23</sup>

**C. Bell Atlantic's Method of Allocating Common Costs is Lawful and Reasonable**

Third, critics ask the Commission to require Bell Atlantic to use a different method for allocating common or shared

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<sup>22</sup> See Johnson Decl., at 35.

<sup>23</sup> Order, **Bell Atlantic Tel. Cos. Revisions to Tariff F.C.C. No. 10, Rates, Terms and Regulations for Video Dialtone Service in Dover Township**, Transmittal Nos. 741, 786, CC Docket No. 95-145, ¶ 27 (rel. June 9, 1995) ("Dover Tariff Order").

costs than the method chosen by Bell Atlantic.<sup>24</sup> Conspicuous by its absence, however, is any suggestion that the particular method utilized by Bell Atlantic is unlawful -- the only test the Commission may apply in this tariff proceeding. Although certain commenters assert that the Commission may and should prescribe a different common cost allocation method for purposes of this tariff,<sup>25</sup> they fail to note that the Commission may do so only if it makes a threshold determination that the particular method used by Bell Atlantic is unlawful;<sup>26</sup> otherwise the Commission may not prescribe a different method without engaging in a rulemaking proceeding.<sup>27</sup>

As Bell Atlantic has explained in detail, Bell Atlantic's method is not only a lawful approach that the Commission has

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<sup>24</sup> AT&T also asserts that Bell Atlantic has not adequately explained its methodology so that AT&T can duplicate Bell Atlantic's calculations. This criticism is mystifying, given that Bell Atlantic has explained its methodology in great detail and in very simple, plain language. See Bell Atlantic Tariff F.C.C. No. 10, Transmittal No. 741, Description & Justification, pp. 3-4 through 3-11, workpapers 5-4, 5-9 (filed Jan. 27, 1995) ("Tariff"); Transmittal No. 741-Amended, Tab 1 (filed May 5, 1995); Tariff Reply, Attachment A, at 1-2, Issue 3; Direct Case, Pre(4), at 8-11.

<sup>25</sup> See MCI Opposition to Direct Case, at 8-9 (filed Nov. 30, 1995) ("MCI Opp."); Adelphia Opp., at 5-6; Cox Opp., at 17-19.

<sup>26</sup> See 47 U.S.C. § 205(a). In the collocation tariff proceedings cited in the Adelphia Opp., at 6 n.9, the Commission made a threshold finding in the first phase of that proceeding that the proposed methodology for applying overhead costs was unlawful before prescribing an adjustment to the rates. See **Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Virtual Collocation**, 10 FCC Rcd 6375, ¶ 101 (1995).

<sup>27</sup> See Administrative Procedures Act, § 553(e), 5 U.S.C. § 553(e).

previously approved in other contexts,<sup>28</sup> it is also a reasonable and logical method that is based on the actual functions that each piece of equipment performs in the network, and the relative proportions of directly attributable voice and video costs.<sup>29</sup>

Moreover, while there is no legal requirement that a carrier use some supposedly "best" allocation method, Bell Atlantic's method is more reasonable than alternatives suggested by its opponents.<sup>30</sup> As Bell Atlantic has previously explained, cost allocation based on minutes of use or an arbitrary 50/50 split between voice and video has no reasoned basis and would make no sense.<sup>31</sup> Cost allocation based on bandwidth<sup>32</sup> is also affirmatively unreasonable:

The differential use of network elements by different services is fundamentally at odds with proposals to assign common costs based on such measures of relative use as bandwidth. Use of such costs would result in unsustainable price differentials and would price some services out of the market entirely. Video services would be assigned roughly 1000 times the fixed costs

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<sup>28</sup> See, e.g., 47 C.F.R. §§ 36.151(c), 64.901.

<sup>29</sup> Direct Case, Issue C, at 39-41. In fact, the only criticism of Bell Atlantic's categorization of each equipment component based on function is MCI's suggestion that Bell Atlantic should be required to assign all network interface device ("NID") costs to video, which Bell Atlantic has already done. See Exhibit A, Issue 3. MCI Opp., at 19-20.

<sup>30</sup> See Direct Case, Issue C.

<sup>31</sup> See Direct Case, Issue A(6), at 20-23 and Issue A(8), at 25-26 (minutes of use), and Issue C(2), at 45 (50/50 allocation); see also, *id.*, Exhibit A, Affidavit of William E. Taylor, Ph.D., ¶¶ 7-10 (minutes of use), and ¶¶ 11-12 (50/50 allocation) ("Taylor Direct Case Aff.").

<sup>32</sup> MCI Opp., at 3.

assigned to voice services. Such a differential would price VDT services out of the market, denying customers the benefit of new and innovative services for which they are willing to pay the cost and denying the LEC the opportunity to expand the use of its network. In addition, use of bandwidth as an allocator of common costs would be inefficient in an environment in which the user could change its bandwidth requirements by preprocessing and compression at the originating end and by storage at the terminating end. Choosing a particular usage-based allocator would thus unreasonably distort the customers' choice of technology in the network and ultimately would raise the total cost of supplying services in the broadband network. As a result, arguments that the Commission should mandate use of bandwidth as an allocator of common costs of the network should be rejected.<sup>33</sup>

In short, commenters have raised no valid criticism of the methodology applied by Bell Atlantic, and instead ask the Commission to impose a different but much less reasonable methodology preferred by the commenter. It is abundantly clear that the primary reason each of these alternative methodologies are preferred by the commenters is that each would lead to an absurdly inappropriate allocation of the shared cost of this robust integrated network, which will support multiple innovative voice, video and data services, to the first new non-telephone service using the network. Their anticompetitive entreaties should be firmly rejected by the Commission.

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<sup>33</sup> Opposition of Bell Atlantic to Petitions to Deny and Response to Comments, Statement and Protest, Exhibit 1, Affidavit of William E. Taylor, Ph.D., ¶ 29 (Aug. 10, 1994), *Application of The Chesapeake and Potomac Tel. Cos.*, W-P-C 6912 (Aug. 11, 1994), see also *id.*, ¶¶ 27-28 (citing R. Pepper, "Through the Looking Glass: Integrated Broadband Networks, Regulatory Policies, and Institutional Change," 4 FCC Rcd 1306, 1313 (1988)).



**D. Bell Atlantic Has Properly Allocated Other Costs to This Video Dialtone Service**

The fourth criticism of Bell Atlantic's cost allocation methods is that Bell Atlantic did not appropriately allocate other costs, such as overhead and start-up costs, to this video dialtone service. This criticism is also unfounded.

The cable industry initially contends that Bell Atlantic underallocated overhead costs to video dialtone service by treating all overhead costs as fixed.<sup>34</sup> They are simply wrong. In accordance with the Commission's rules, Bell Atlantic allocated to video dialtone all costs that could be directly attributed to that service, including certain costs the cable industry has mischaracterized as overhead, such as administration, maintenance and powering. In addition, Bell Atlantic has appropriately allocated a portion of embedded plant to this new video dialtone service, as direct costs, by applying a factor derived from company accounting records to investments for land and buildings, power and common equipment, and poles and conduits.<sup>35</sup> It was only after including these categories of costs as direct costs that the company additionally allocated to video dialtone a portion of all remaining "overhead" costs, which could not be directly allocated

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<sup>34</sup> NCTA Opp., at 17-18; Adelphia Opp., at 15-17.

<sup>35</sup> See Direct Case, Issue Pre(4), at 9.

on a cost-causal basis and which do not vary with the introduction of this new service.<sup>36</sup>

As Dr. Taylor explains, the statistical analyses proffered by cable fail to show that Bell Atlantic's remaining overhead costs will vary with the introduction of video dialtone service. The relationship between overhead and lines (or revenues) among the seven Bell Atlantic operating companies, which offer roughly the same number and type of services, says nothing about whether plant non-specific and corporate expense overhead would increase more if a new subscriber ordered video dialtone rather than telephony service.<sup>37</sup>

Notwithstanding the cable industry's assertions to the contrary,<sup>38</sup> Bell Atlantic has not claimed that there will be no increase in certain expenses that cable categorizes as overhead despite the introduction of this new service.<sup>39</sup> It is precisely because certain new costs will be incurred that any expenses that are directly attributable to video dialtone service have been attributed to this new service. Moreover, overhead expenses that are not directly attributable to video dialtone service are not

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<sup>36</sup> See, e.g., Tariff, Description & Justification, Section 3.0. As a matter of economic principles, the only costs that qualify as overhead, by definition, are those that cannot be identified as cost-causally related to a specific service. See also Supplemental Taylor Aff., ¶ 9.

<sup>37</sup> Supplemental Taylor Aff., ¶¶ 11-14.

<sup>38</sup> Cox Opp., at 30-31; NJCTA Opp., at 13-14; Adelphia Opp., at 17-18.

<sup>39</sup> Johnson Decl., at 23; see also MCI Opp., at 21.

expected to increase disproportionately as a result of the introduction of this new service; consequently, it would be inappropriate to allocate an additional disproportionate share of overhead to video dialtone service.

MCI erroneously contends that this new video dialtone service should be forced to bear the same overhead loading as "comparable services."<sup>40</sup> It is perfectly valid in a competitive market to recover different proportions of corporate overhead expense from even roughly comparable services to meet marketplace demands.<sup>41</sup>

In any event, the services MCI identifies are not comparable. Video dialtone is a new competitive service and Bell Atlantic is a new entrant seeking to compete in the video delivery market with such established competitors as cable, direct broadcast satellite, video rental stores, and broadcast stations. As Dr. Taylor explains, in an unregulated competitive market, the initial "mark-up" (or price above incremental cost) for a fledgling competitive service will not be the same as the mark-up for an established service.<sup>42</sup> By seeking to recover as much overhead from the newly competitive service as from the established service, the company is likely to price its newly competitive service above the

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<sup>40</sup> MCI Opp., at 22. Again, overhead loadings reflect only those costs not assigned as direct costs.

<sup>41</sup> Supplemental Taylor Aff., ¶ 16.

<sup>42</sup> *Id.*, ¶ 15.

level that will allow it to compete effectively with the incumbent providers.<sup>43</sup>

Second, critics also complain that Bell Atlantic has not required this initial video dialtone service offering to bear all of the start-up costs associated with the company's entry into the video dialtone business.<sup>44</sup> It would be inappropriate, anticompetitive and contrary to basic economic principles, however, to force Bell Atlantic's initial video dialtone service offering in Dover Township to absorb and recover all of Bell Atlantic's start-up costs to enter the video delivery market. The problem is not only identifying the amount of start-up expenses for video dialtone service that Bell Atlantic has incurred, but isolating those expenses that relate only to *this* initial service offering in Dover Township. Most of the legal, planning, research and development, and similar start-up expenses incurred by Bell Atlantic as it prepares to enter the video delivery market have been incurred because Bell Atlantic is entering the video dialtone service business in multiple locations, not just in Dover Township.<sup>45</sup> Every video dialtone service offering by Bell Atlantic will share the benefits of these sunk costs, and no segregable costs can be

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<sup>43</sup> See Direct Case, Exhibit B, Declaration of Robert J. Rider, at 2-3 (Oct. 25, 1995).

<sup>44</sup> See Cox Opp., at 19, NJCTA Opp., at 9-10.

<sup>45</sup> See Direct Case, Issue D, at 51-52.

identified that only benefit this video dialtone service offering.<sup>46</sup>

Nevertheless, as Dr. Taylor explains, no cross-subsidization concerns arise. Because start-up costs are by definition non-recurring costs that are sunk:

they are certainly not part of the incremental cost of VDT subscription or usage, and they are not even a service-specific fixed cost (because they are sunk). It follows that start-up costs are not included in a cross-subsidy test: a firm that ignores sunk costs in its pricing decisions cannot be said to engage in cross-subsidy.<sup>47</sup>

Loading all of these sunk costs on this initial fledgling service would be both inappropriate and anticompetitive.<sup>48</sup>

Third, MCI contends that Bell Atlantic should be required to recover through its prices for this video dialtone service the costs of any "spare" fiber capacity.<sup>49</sup> The prices here were set above incremental costs of this service, as appropriate under the Commission's tariff rules.<sup>50</sup> Costs of spare network capacity are assigned in accordance with the requirements of Part 36 and Part 69 of the Commission's rules.

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<sup>46</sup> Supplemental Taylor Aff., ¶ 24.

<sup>47</sup> *Id.*, ¶ 23 (citation omitted).

<sup>48</sup> The Commission's tariff rules recognize these principles and require cost recovery to be based on forward-looking incremental costs or, in the case of video dialtone, defined direct costs.

<sup>49</sup> MCI Opp., at 18.

<sup>50</sup> See Direct Case, Pre(2) and Pre(3).

Finally, AT&T renews its previous criticism that Bell Atlantic should reduce prices for other access services because it has reapportioned to video dialtone service shared or embedded investments that were previously allocated to voice service.<sup>51</sup> The Commission has never accepted AT&T's repricing theory in other contexts.<sup>52</sup> As explained above, however, this video dialtone service will bear a portion of existing land, building, power and common equipment costs because Bell Atlantic assigns these investments to the direct cost of video dialtone.<sup>53</sup>

**E. Bell Atlantic Has Properly Redacted Proprietary Vendor Pricing Information**

MCI and AT&T repeat objections to Bell Atlantic's redaction of certain proprietary vendor pricing information. Bell Atlantic has previously addressed these arguments in detail<sup>54</sup> and will not burden the Commission by repeating its responses here.

MCI, however, takes issue with Bell Atlantic's representation that the only information Bell Atlantic has redacted

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<sup>51</sup> AT&T's Comments on Direct Case, at 8 (filed Nov. 30, 1995) ("AT&T Comments").

<sup>52</sup> The Commission has never required LECs to adjust prices of existing services because of the introduction of new services. The Commission's rules clearly allow, and even require, new service prices to include contribution above incremental cost. VDT Recon Order, ¶ 218. The requirement to reduce rates for other services because of expected contribution from a new service would discourage LECs from bringing new services to market.

<sup>53</sup> See *supra* at 15.

<sup>54</sup> See Direct Case, Introduction and Summary, at 6-12; see also Bell Atlantic's Opposition to Motion for Extension of Time (filed Nov. 22, 1995).

is a limited set of vendor-specific prices for subcomponents of certain pieces of equipment used in the Dover system (or information that would allow those prices to be calculated), asserting that investment information for entire rate elements has been redacted.<sup>55</sup> Contrary to MCI's claims, Bell Atlantic has publicly disclosed, in unredacted form, aggregate investment and expense information for each rate element, and for each facility and piece of equipment (HDT, ONU, etc.).<sup>56</sup> The only information that has been redacted -- and that would be disclosed only under the Nondisclosure Agreement provided by Bell Atlantic -- are the prices for the individual *subcomponents* of certain pieces of equipment.<sup>57</sup>

As Bell Atlantic has previously noted, the only reason any party would need access to this granular level of detail is to verify Bell Atlantic's arithmetic, by assuring themselves that the sum of the individual subcomponent prices is equal to the aggregate

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<sup>55</sup> MCI Opp., at 6.

<sup>56</sup> For a guide to the location of the aggregate investment and expense information for each rate element, facility and piece of equipment covered by this tariff, see Exhibit F.

<sup>57</sup> This case is very different from that presented by a recent Southwestern Bell Telephone Company request for confidential treatment of certain cost support data. See Letter from Regina M. Keeney, Chief, Common Carrier Bureau, to Thomas A. Pajda, Esq., Southwestern Bell Tel. Co., dated Nov. 28, 1995, at 2-3 (DA 95-2395). Unlike that case, Bell Atlantic here has made a particularized showing both of the competitive significance of the redacted data and specific examples of likely competitive harm, see Direct Case, Introduction and Summary at 9-11. Moreover, as explained, Bell Atlantic has disclosed all aggregated data and protected only costs for individual expense items.

investment already publicly disclosed for that piece of equipment. Because Bell Atlantic has also publicly disclosed its categorization of each piece of network equipment as voice only, video only or shared investment, *down to the subcomponent level*,<sup>58</sup> the parties have publicly available to them all information they need to review and challenge Bell Atlantic's cost allocations and pricing for this tariff.

### **III. Provision of Digital Converters and Network Interface Software are Non-Regulated Services**

One of the video information providers that has reserved capacity on the Dover system, Rainbow Programming Holdings, Inc., asks the Commission to reverse longstanding Commission policy and re-regulate provision of certain customer premises equipment and software. Rainbow's argument is contrary to public policy and is based on incorrect and misleading assertions of fact. Moreover, Rainbow's request is beyond the scope of this proceeding, because the Commission could not change its policy absent a rulemaking proceeding.<sup>59</sup>

The Commission, after lengthy proceedings, has concluded that it is not "appropriate or necessary to impose nondiscrimination requirements on enhanced and other nonregulated services"

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<sup>58</sup> See Transmittal No. 741-Amended, Tab 8 (filed May 5, 1995).

<sup>59</sup> See Administrative Procedures Act, § 553(e), 5 U.S.C. § 553(e).



provided in connection with video dialtone service.<sup>60</sup> Rainbow has made no showing that would give the Commission cause to revisit that decision.

Rainbow asserts that the Commission must require Bell Atlantic to tariff provision of a particular proprietary software to all video providers, because video providers are required to use this software in order to connect to the Dover network.<sup>61</sup> It appears that Rainbow has either forgotten, or has misunderstood or misinterpreted, the information that Bell Atlantic has conveyed to Rainbow.

Bell Atlantic has repeatedly informed all potential programmer-customers, including Rainbow, that they are required to provide the software to interface with the Dover system's Video Administration Module ("VAM"), the intelligent network system

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<sup>60</sup> See **Telephone Company-Cable Television Cross-Ownership Rules, §§ 63.54 - 63.58**, 7 FCC Rcd 5781, ¶ 92 (1992); see also **Detariffing of Billing and Collection Services**, 102 FCC 2d 1150, ¶¶ 37-38 (1986); Order on Reconsideration, **Application of US West Communications, Inc.**, W-P-C 6868, ¶ 23 (rel. Nov. 15, 1995) (upholding US West decision to provide billing and marketing services to one video dialtone provider but not another, because carrier is "not obligated to provide nonregulated services, such as billing and marketing, on a nondiscriminatory basis.") (citations omitted).

<sup>61</sup> Opposition of Rainbow Programming Holdings, Inc. to Bell Atlantic Direct Case, at 15-20 (Nov. 30, 1995) ("Rainbow Opp.").